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No. 90-333

In The

Supreme Court of the United States

October Term, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,

Petitioner,

vs.

JOHN GILBERTSON, JOHN V. REITZ, and ANTHONY CATALAN, et al.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONSE TO BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

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QUESTIONS PRESENTED

1. Is there a conflict among the circuits on the statute of limitations for 10b-5 actions?

2. Does the lack of a uniform statute of limitations for 10b-5 actions result in chaos and confusion?

3. Would a federal statute of limitations for 10b-5 actions barring any claims more than three years after the violation, regardless of when the injured party discovered the violation, further the policy and objectives of a private right of action under Rule 10b-5?

4. Should an outright change in the statute of limitations, which has not been "foreshadowed," be applied retroactively to bar claims which were viable under the existing statute of limitations at the time the suit was filed?

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STATEMENT OF THE CASE

Factual Background

Respondents accept petitioners' Statement of the Case with the following corrections. Petitioners did not "allegedly assist" in preparing the offering memorandum, they prepared it totally. Petitioners prepared all the closing documents, the offering memorandum, and the tax opinion. Petitioners prepared instructions for the

salesmen. Petitioners received investors' funds and made disbursements.

The limited partnership were *very* fraudulent. In several, the assets which were supposed to be purchased at closing with the investors' money were not purchased at all. Fraudulent paperwork was prepared to show nonexistent purchases. The funds were stolen. Each partnership purchased a software tape purportedly worth about $2,000,000. None of the seven software tapes ever generated more than trace amounts of revenue. The appraisals supplied to investors were lies.

The general partners were friends and close business associates of the promoters. If they became aware of facts suggesting the fraudulent nature of the partnerships, they certainly did not communicate them to the respondents, limited partners. They did the opposite. They permitted the promoters to send the investors a series of "expert reports" explaining the partnership problems and lack of profitability. The explanations appeared reasonable, and never, of course, suggested fraud.

When the IRS challenged the valuations of the partnership assets, the general partners were forced to hire outside counsel. The lawyers discovered the fraud while investigating the value of the assets. Because of the involvement of outside counsel and the imminence of IRS problems, the facts suggesting fraud were finally communicated to the respondents.

Suit was filed within a year after plaintiffs learned of those facts.

Proceedings Below

Respondents accept petitioner's summary of the proceedings in the district and circuit courts.

REASONS FOR DENYING THE WRIT

I.

THERE HAS ALWAYS BEEN CONFLICT WITHIN AND AMONG THE CIRCUITS ABOUT THE STATUTE OF LIMITATIONS FOR 10b-5 ACTIONS; THE THIRD CIRCUIT DECISION IN *IN RE DATA ACCESS SYSTEMS SECURITIES LITIGATION*, 843 F.2d 1537 (3d Cir.) (en banc), cert. denied, ___ U.S. ___, 109 S.Ct. 131, 102 L.Ed.2d 103 (1988), HAS NOT INCREASED THE CONFLICT.

Before *In Re Data Access, supra*, all federal courts looked to state law for the applicable statute of limitations. There were fifty different rules creating differences within and between circuits. *In Re Data Access* standardizes the rule within the Third Circuit. To that extent, *In Re Data Access* has reduced conflict, not increased it.

The Third Circuit read this Court's decisions in *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), and *Del Costello v. Teamsters*, 462 U.S. 151 (1983), as permission to look to federal law for the statute of limitations in 10b-5 cases. Those cases did invite federal courts to consider federal law in determining the most analogous statute of limitations for federal causes of action. Nothing in those cases suggested a preference for federal law unless federal law is more analogous than state law. There are just more analogies to consider.

The fact that one circuit has chosen a federal law as the appropriate analogy in 10b-5 cases does not create a conflict between the circuits. It simply reflects the fact that this Court's decisions in *Agency Holding Corp.* and *Malley-Duff* make more choices available.

II.

THE PRESENT SITUATION IS NOT "CHAOTIC". Brief for Petitioner, p. 8.

For reasons stated above, the situation after *In Re Data Access, supra,* is, if anything, less complicated than it was before the decision. There are decisions in each federal district deciding which state statute of limitations applies to 10b-5 actions. Litigants bringing 10b-5 actions are not confused about the applicable statute of limitations. We doubt that any judicial time or energy is spent deciding which statute of limitations applies.

There is undoubtedly forum shopping where a 10b-5 action may be brought in more than one state and the statutes of limitations differ. The fact of forum shopping is not an imposition on the federal court system, and it does not require this Court's attention. If the case is brought in a proper forum, it is unimportant that the statute of limitations was a consideration.

A national statute of limitations for 10b-5 actions would be conceptually tidy and, for that reason, desirable. As will be discussed next, petitioner's proposal for conceptual tidiness would be purchased at the price of greatly reducing the effectiveness of 10b-5 to deter and remedy securities fraud.

III.

A STATUTE OF LIMITATIONS FOR SECURITIES FRAUD WHICH CANNOT BE TOLLED FOR CONCEALMENT IS UNFAIR AND ONLY PARTIALLY EFFECTIVE.

In *In Re Data Access*, 843 F.2d 1537, 1550 (3d Cir. 1988), the Third Circuit imposed a three year statute of limitations regardless of defendant's efforts at concealment and plaintiff's inability to discover the fraud:

> Accordingly, we have decided that the proper period of limitations for a complaint charging violation of section 10(b) and Rule 10b-5 is one year after the plaintiff discovers the facts constituting the violation, and in no event more than three years after such violation.

843 F.2d 1550. The last clause appears to say that the defendant who has committed fraud wins if he or she successfully conceals the fraud for three years, or if the plaintiff, with or without fault on his or her part, remains ignorant of the fraud for three years.

As the present case demonstrates, where promoters commit securities fraud, they do not intend to be immediately sued or indicted. They intend to enjoy their ill-gotten gain. Fraud is by nature concealment of the truth by misrepresentation or omission. A statute of limitations which cannot be tolled for successful concealment, and which, in effect, rewards successful concealment, is not a desirable statute of limitations for a fraud action.

This Court has frequently recognized that a fraud statute of limitations must be tolled where the fraud has been concealed or where the plaintiff has failed to discover the fraud through no fault of his or her own. *Bailey*

v. Glover, 88 U.S. 342 (1875); *Exploration Co. v. United States*, 247 U.S. 435 (1917); *Holmberg v. Armbrecht*, 327 U.S. 392 (1945); and *American Pipe and Construction Co. v. Utah*, 414 U.S. 538 (1974).

Bailey, supra, was a fraud action in equity subject to a statute of limitations in the "Bankrupt Act" stating that "no suit in law or in equity shall in any case be maintained . . . unless brought within two years. . . . " 88 U.S. at 348-349. The Court held that the equitable rule that "the bar of the statute does not begin to run until the fraud is discovered" also applies to statutes of limitations in cases at law.

> We also think that in suits in equity the decided weight of authority is in favor of the proposition that where the party injured by the fraud remains in ignorance of it without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party.
>
> * * *
>
> But we are of opinion, as already stated, that the weight of judicial authority, both in this country and in England, is in favor of the application of the rule to suits at law as well as in equity. And we are also of opinion that this is founded in a sound and philosophical view of the principles of the statutes of limitation. They were enacted to prevent frauds; to prevent parties from asserting rights after the lapse of time had destroyed or impaired the evidence which would show that such rights never existed, or had been satisfied, transferred, or extinguished, if they ever did exist. To hold that by concealing

> a fraud, or by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statute of limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure. And we see no reason why this principle should not be as applicable to suits tried on the common-law side of the court's calendar as to those on the equity side.

88 U.S. at 348-349.

In *Exploration Co., supra*, the defendant "talked very freely" about the fraud by which he had obtained and concealed an illegal land patent after the six year statute of limitations on suits to vacate patents had expired. 247 U.S. at 445-446. The government sued, asserting the rule in *Bailey, supra*. This Court reaffirmed *Bailey*, holding that the statute of limitations had been tolled, even though it made no provision for tolling.

> When Congress passed the act in question the rule of *Bailey v. Glover* was the established doctrine of this court. It was presumably enacted with the ruling of that case in mind. We cannot believe that Congress intended to give immunity to those who for the period named in the statute might be able to conceal their fraudulent action from the knowledge of the agents of the Government. We are aware of no good reason why the rule, now almost universal, that statutes of limitations upon suits to set aside fraudulent transactions shall not begin to run until the discovery of the fraud, should not apply in favor of the Government as well as a private individual. It is not our belief that Congress intended that the Government should be deprived of title to public lands by those who added to the fraud by which they were

> obtained, artifices which enabled them to conceal the fraudulent manner in which they were secured until the action was supposed to be barred by the lapse of six years.

247 U.S. at 449-450.

The rule in *Bailey* was again reaffirmed in *Holmberg, supra.*

> And so this Court long ago adopted as its own the old chancery rule that where a plaintiff has been injured by fraud and "remains in ignorance of it without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party." *Bailey v. Glover*, 21 Wall. 342, 348; and *see Exploration Co. v. United States*, 247 U.S. 435; *Sherwood v. Sutton*, 5 Mason 143.
>
> This equitable doctrine is read into every federal statute of limitation.

327 U.S. at 397.

In *American Pipe and Construction Co., supra*, this Court held that public bodies and state agencies in Utah, purported class members in an unsuccessful antitrust class action for damages, could intervene in a similar antitrust action for damages brought by the State of Utah, after the statute of limitations had expired. The class action was timely filed, but class status was denied after the statute had expired. The potential class members then intervened individually in the action brought by the State. In so holding, this Court reaffirmed *Holmberg*, emphasizing that the power of the federal courts to toll a

federal statute of limitations is "deeply rooted in our jurisprudence."

> Similarly, in cases where the plaintiff has refrained from commencing suit during the period of limitation because of inducement by the defendant, *Glus v. Brooklyn Eastern Terminal*, 359 U.S. 231, or because of fraudulent concealment, *Holmberg v. Armbrecht*, 327 U.S. 392, this Court has not hesitated to find the statutory period tolled or suspended by the conduct of the defendant. In *Glus, supra*, the Court specifically rejected a contention by the defendant that when 'the time limitation is an integral part of a new cause of action . . . that cause is irretrievably lost at the end of the statutory period.' 359 U.S., at 232. To the contrary, the Court found that the strict command of the limitation period provided in the federal statute was to be suspended by considerations '[d]eeply rooted in our jurisprudence.' Ibid.
>
> These cases fully support the conclusion that the mere fact that a federal statute providing for substantive liability also sets a time limitation upon the institution of suit does not restrict the power of the federal courts to hold that the statute of limitations is tolled under certain circumstances not inconsistent with the legislative purpose.

414 U.S. at 559.

Despite this Court's repeated insistence on interpreting all federal statutes of limitations in fraud cases to permit tolling where the plaintiff is unaware of the fraud through no fault of his or her own, the petitioner is asking this Court to impose on all 10b-5 actions a statute of limitations which, by its terms, appears to preclude any such flexibility. The result would be to reduce the

scope of 10b-5, to reward perpetrators of securities fraud who are able to conceal it, and to deny the remedy to defrauded investors who are unaware of the fraud through no fault of their own.

IV

THE STATUTE OF LIMITATIONS SHOULD NOT BE RETROACTIVELY SHORTENED TO BAR RESPONDENTS' FRAUD CLAIMS.

If this Court issues a writ of certiorari, whether the statute of limitations should be changed retroactively to bar respondents' fraud claims will be a major issue.

CONCLUSION

This Court denied certiorari when *In Re Data Access* was decided. The rule in that case offers simplicity where it is not needed. The statute of limitations for 10b-5 actions is very clear in every state. The simplicity offered by uniform application of the *In Re Data Access* rule would be purchased at the cost of this Court's historic insistence that statutes of limitations for fraud be tolled for investors who, through no fault of their own, have not discovered the fraud.

This Court's decisions in *Malley-Duff* and *Del Costello* have given the lower courts new options for finding the appropriate statute of limitations for federal causes of action. The Third Circuit rule in *In Re Data Access*, recently rejected by the Ninth and Eleventh Circuits, demonstrates that the lower courts are just starting to

consider whether a uniform rule in 10b-5 cases is necessary, and, if so, what it should be. *Nesbit v. McNeil*, 896 F.2d 380, 384 (9th Cir. 1990); *Smith v. Duff and Phelps, Inc.*, 891 F.2d 1567, 1569-70 (11th Cir. 1990).

The choices presented by this case are not good ones: reaffirming the multiplicity of state statutes or adopting a uniform federal statute of limitations which prohibits tolling. If a uniform federal statute of limitations is a good idea, the lower courts will eventually present this Court with better alternatives.

Respectfully submitted,

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